paragon

John Heron

Managing Director – Mortgages, Paragon

Q1 2018 **HIGHLIGHTS**

- Landlords resize property portfolios
- Portfolio gearing falls to all-time low
- Specialist lenders take on growing role

LANDLORDS AND LENDERS ADAPT THEIR APPROACH

Our Q1 2018 PRS Trends survey highlights a number of interesting changes in behaviour as landlords and lenders navigate their way through the regulatory and fiscal changes affecting the buy-to-let sector.

First, we see the potential for a growing polarisation between small and larger scale landlords as landlords with between 6 and 20 properties in their portfolio increase from 35% to 39% of the total and those in the 3 to 5 property bracket fall from 26% to 24%.

Landlords at the top end have also been resizing, with a fall in the proportion of those who have over 50 properties in their portfolio, down from 6% to 4% of the total, and an overall reduction in the average portfolio size from 13.1 to 11.6 properties.

Alongside portfolio resizing, landlords also report reductions in portfolio gearing and rent increases.

Average portfolio gearing which measures the loan to value ratio of a property portfolio, reduced from 35% to 32% compared with three months ago, falling from a peak of 43% to hit its lowest level ever since Paragon's PRS Trends survey began.

Meanwhile, almost a quarter (24%) of landlords reported that they had increased rent in the last three months and that they were spending an increased proportion of their rental income on mortgage costs, up to 30% of income from 26% at the end of 2017.

For lenders, the PRA changes point to greater scrutiny of mortgage applications and increased specialisation.

For example, almost all landlords (80%) reported an increase in documentation requirements and mortgage processing timescales when asked about their experience in applying for a buy-to-let mortgage after the introduction of the second phase of the PRA underwriting standards on 30 September 2017.

Portfolio landlords with four or more mortgaged properties went even further, with 46% pointing to a reduction in the number of lenders available for them to choose from.

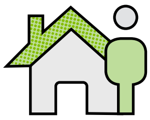
Taken together, these changes point to a growing role for buy-to-let specialist lenders, opening the way for those with a broader underwriting expertise and more extensive product range to step up their support for landlords and increase their market share.

John Heron, Managing Director
Mortgages, Paragon

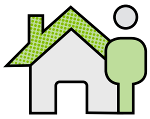
OUR LANDLORD PANEL

Our panel is an experienced group of 203 buy-to-let landlords, with 83% of the 203 landlords surveyed having been residential landlords for more than ten years and 44% having been involved for more than 20 years.

Three quarters (75%) of landlords surveyed in Q1 2018 are classed as professional – owning three or more properties – and our sample is both an accurate reflection of the rented residential sector and Paragon's customer base of residential landlords.



83% LANDLORDS FOR 10 YEARS +



44% LANDLORDS FOR 20 YEARS +

75% OWNING THREE OR MORE PROPERTIES

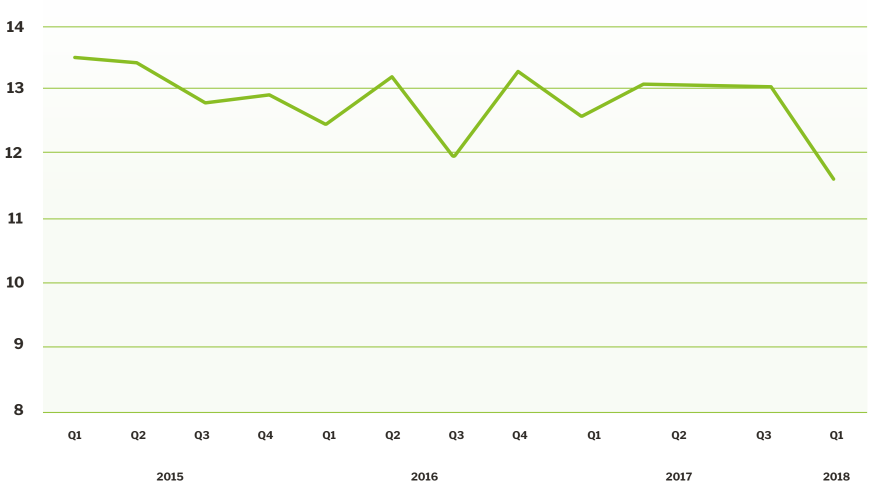
PORTFOLIO SIZE

On average, residential landlords have 11.6 properties in their portfolio in Q1 2018, down quite sharply from an average of 13.1 properties three months ago.

Landlords with between 6 and 20 properties have increased from 35% to 39% of the total, following a fall in those with 3 to 5 properties from 26% to 24%. While this suggests the potential for polarisation between small and larger scale landlords, those with more than 50 properties have also been trimming back, reducing from 6% to 4% of the survey population.

The average portfolio value for all landlords was £1.63 millon.

Average number of rented residential properties in portfolio

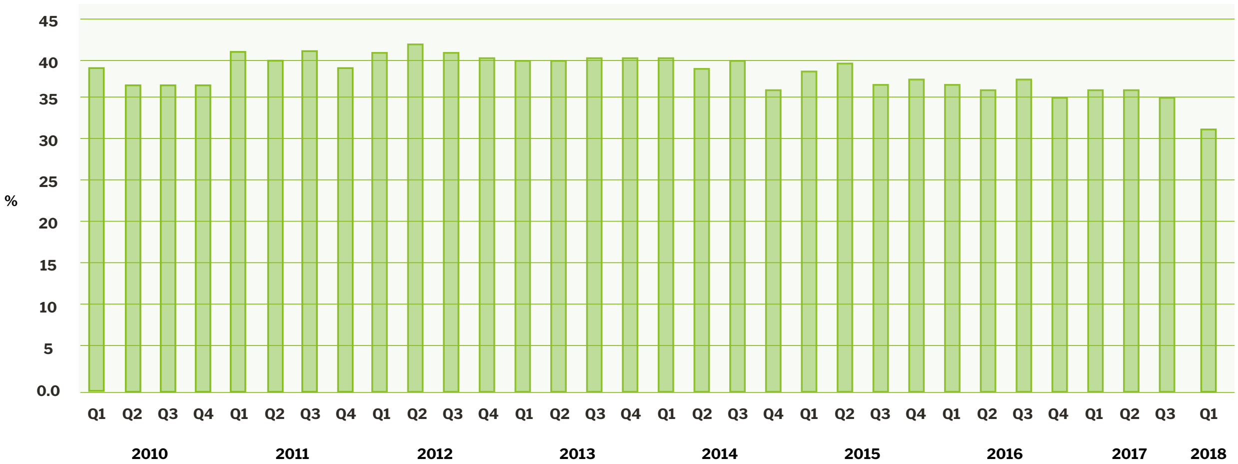


GEARING

Landlords continued to reduce the proportion of their borrowing relative to their portfolio value, with average loan to value falling from 35% to 32% this quarter.

This is the lowest level of portfolio gearing recorded since the survey began in 2001. Gearing peaked at 43% in 2012 and has been on a downward trend since, suggesting landlords are committed to maintaining borrowing at manageable and sustainable levels.

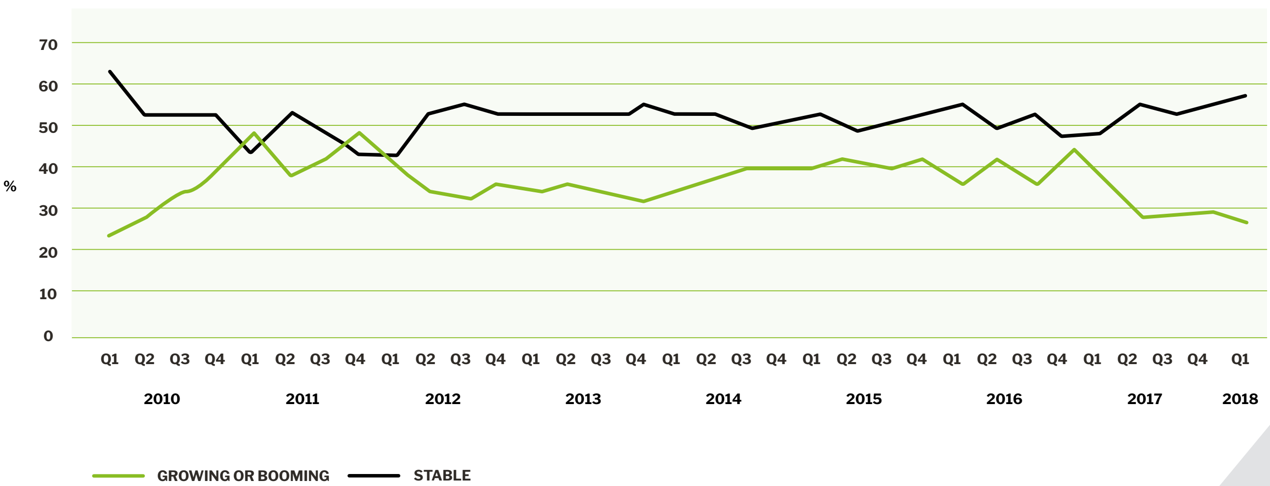
Average gearing of investment property portfolios



TENANT DEMAND

Tenant demand remains strong but a lower proportion of landlords (28%) describe demand as growing or booming compared to three months ago (30%). The majority of landlords (58%) describe tenant demand as stable.

Chart title: Proportion of landlords who say tenant demand is growing or booming

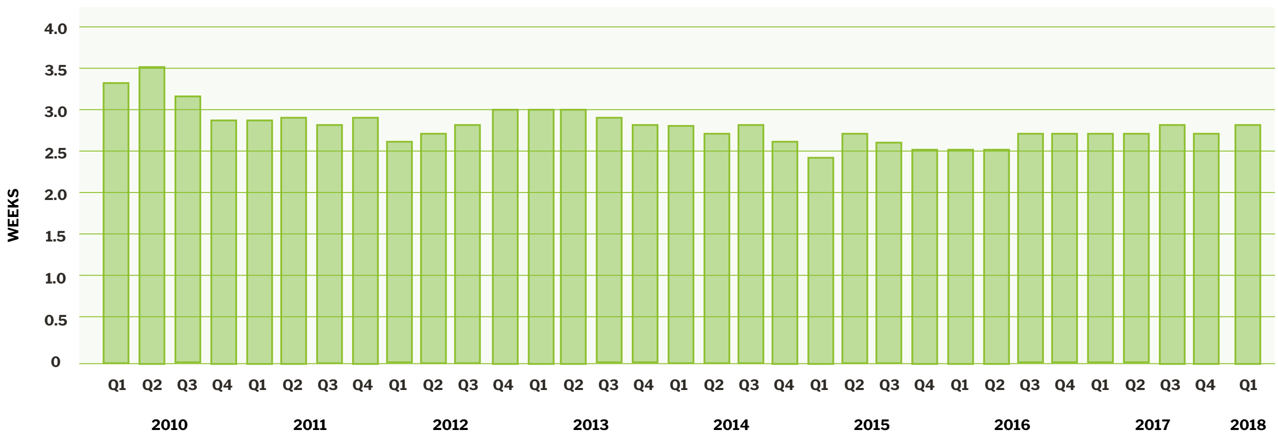


VOID PERIODS

The overall average void period for landlords is 2.8 weeks, up from 2.7 weeks in the last survey.

The void period which measures how long the average property is empty in a year has been fairly stable at between 2.6 weeks and 3 weeks for most of the last 16 years, moving outside of this range only in 2009 and 2010.

Average void period



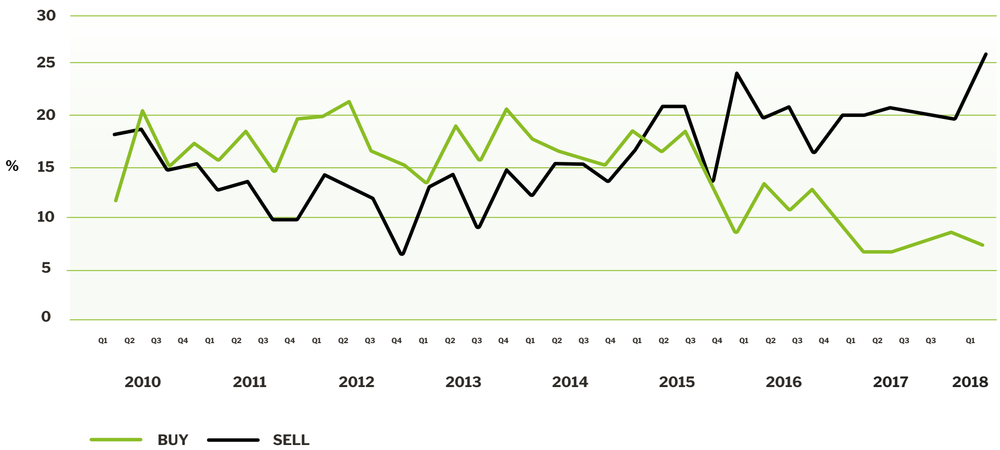
BUYING VS. SELLING EXPECTATIONS

Less than one in ten landlords (8%) say that they expect to purchase buy-to-let property in the next quarter with more than nine out of ten (92%) saying they do not. Landlords' propensity to buy property has fallen from 9% last quarter to 8% this time round.

Meanwhile more than a quarter (26%) of landlords expect to sell some or all of their buy-to-let property in the next quarter, up from 22% and the second increase in succession.

Interestingly, the gap between those who plan to buy and those expecting to sell has increased again and is now at its widest since 2009.

Proportion of landlords expecting to buy and sell property in the next quarter

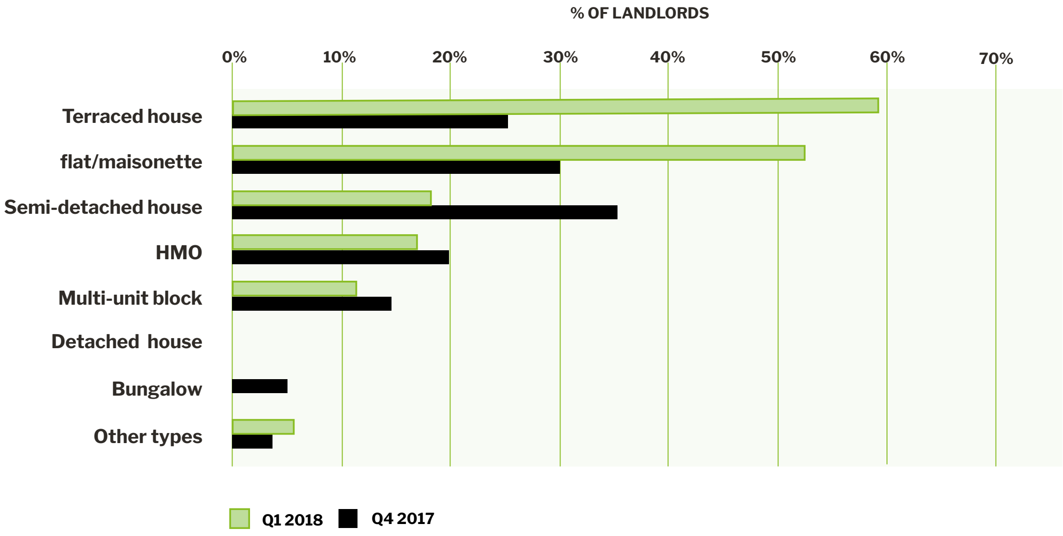


PROPERTY TYPES

For those landlords who plan to buy property in the next quarter, terraced houses are in the highest demand favoured by six out of ten (60%). Flats are next most popular, sought after by 52% of landlords.

However, semi-detached are less popular that three months ago, with only 17% of landlords showing interest compared with 35% last time round.

Type of property expected to purchase



CHANGES TO THE BUY-TO-LET APPLICATION PROCESS

In this quarter, we asked landlords who had applied for a buy-to-let mortgage following the introduction of the second phase of the PRA underwriting changes on 30 September 2017 to tell us about their experience.

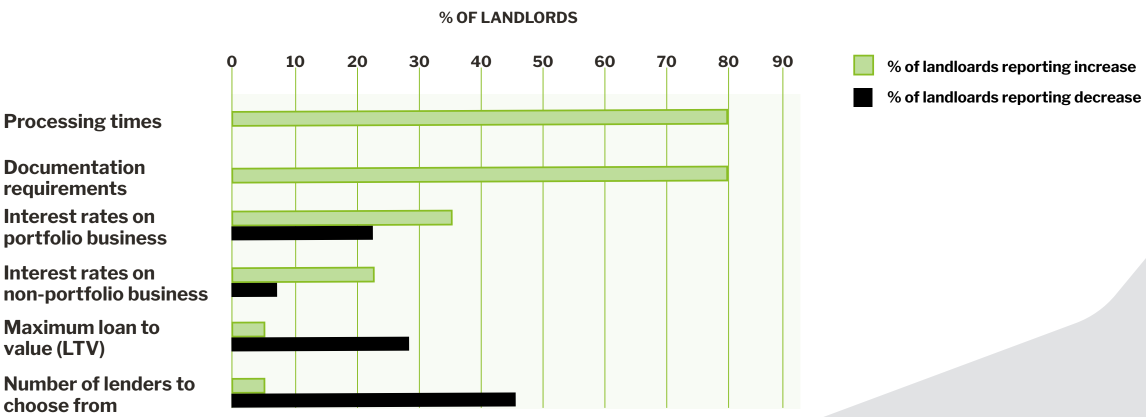
The vast majority (80%) told us they had noticed an increase in documentation requirements and mortgage processing times.

Just over one third (34%) said they had noticed an increase in interest rates on portfolio landlord business.

In addition, three out of ten landlords reported that loan-to-value ratios had fallen.

Most interesting, while non-portfolio landlords on the whole hadn't noticed any change in the number of lenders they could choose from, 45% of portfolio landlords said they now had less choice.

Changes to the buy-to-let application process

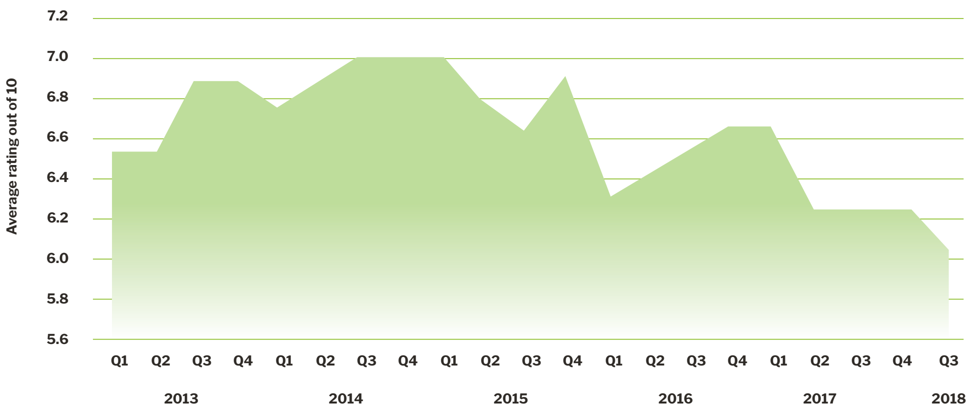


OVERALL PROSPECTS FOR THE PRS

When asked to score the prospects for the private rented sector in the next 12 months, landlords returned an average score of 6.1 out of ten. This is down from 6.3 three months ago and represents the lowest level since this question was introduced in 2012.

Although the figure has never risen above 7.0, it has been on a downward trend since Q1 2017 and clearly indicates a dampening of landlord optimism as the various fiscal and regulatory changes take effect.

Overall prospects for the PRS in the next 12 months



ABOUT PARAGON

Paragon is a leading provider of buy-to-let mortgages for landlords with portfolios both big and small through its portfolio and non-portfolio range.

Paragon lends to individuals and limited companies and has mortgages suitable for single self-contained properties, as well as HMOs and multi-unit blocks. Paragon can accommodate higher aggregate lending limits and more complex letting arrangements including local authority leases and corporate leases along with ASTs.

Paragon introduced its first product aimed at the professional property investor in 1995 and is a member of UK Finance, the Intermediary Mortgage Lenders Association (IMLA), National Landlords Association (NLA) and the Association of Residential Letting Agents (ARLA).

Paragon Bank PLC is a subsidiary of the Paragon Banking Group PLC which is a FTSE 250 company based in Solihull in the West Midlands. Established in 1985, Paragon Banking Group PLC has over £12 billion of assets under management and manages over 450,000 customer accounts.